

ST 99-24

Tax Type: Sales Tax

Issue: Responsible Corporate Officer – Failure to File or Pay Tax

**STATE OF ILLINOIS
DEPARTMENT OF REVENUE
OFFICE OF ADMINISTRATIVE HEARINGS
CHICAGO, ILLINOIS**

**THE DEPARTMENT OF REVENUE
OF THE STATE OF ILLINOIS**

v.

"HYERONIMOUS MONK", as responsible
officer of "Ashram Building Co.",

Taxpayer.

Docket No. 98-ST-0000
IBT No. 0000-0000
NPL: 0000
NOD: 0000

John E. White,
Administrative Law Judge

RECOMMENDATION FOR DISPOSITION

Appearances: Gust Dickett, of Romanoff & Dickett, on behalf of "Hyeronimus Monk"; Mark Dyckman, Special Assistant Attorney General, on behalf of the Illinois Department of Revenue.

Synopsis:

This matter arose when "Hyeronimus Monk" ("taxpayer" or "Monk") protested a Notice of Penalty Liability and a Notice of Deficiency the Illinois Department of Revenue ("Department") issued to him as a responsible officer of "Ashram Building Co." d/b/a "Sal Monella's" Restaurant. Notice of Penalty Liability ("NPL") number 0000 assessed a penalty equal to the unpaid Retailers' Occupation Tax ("ROT") liability of the corporation, as measured by the gross receipts the corporation earned from sales during the months of 1/93, 7/93 through and including 12/93, 1/94 through and including 2/94, 5/94 and 7/94. Notice of Deficiency ("NOD") number 0000 proposed to assess tax equal

to the amount of Illinois income taxes withheld from the wages of the corporation's employees during 1993, but never paid to the Department.

A hearing was held at the Department's offices in Chicago, in April 1999. At hearing, taxpayer introduced evidence consisting of its books and records, and the testimony of taxpayer, as well as that of another employee of the corporation. I have reviewed the evidence adduced at hearing, and I am including in this recommendation findings of fact and conclusions of law. I recommend that the penalties and deficiencies be assessed against taxpayer.

Findings of Fact:

1. "Ashram Building Co." (hereinafter "ABC") is a corporation that conducted business in Illinois as "Sal Monella's" Restaurant. *See* Department Ex. 1. The restaurant was located at 1111 West 195th Street in "Someplace", Illinois. Department Ex. 3 (Illinois Business Registration application form for "ABC").
2. "ABC" filed ROT returns regarding the periods for which personal liability penalties were assessed against taxpayer. Department Ex. 1; Taxpayer Ex. 8. The tax shown to be due on those returns, however, was not paid, generally because the "ABC" checks drawn to pay the amounts of tax due were dishonored when presented for payment. *See* Taxpayer Ex. 8 (exhibit contains copies of "ABC's" returns filed and copies of "ABC" checks drawn to pay the amounts of tax due).
3. "ABC" withheld amounts of Illinois income tax from its employees' wages during 1993, and the amounts withheld were not paid over to the Department. Taxpayer 4; Department Exs. 1-2.
4. Taxpayer was the president of "ABC". Department Ex. 3; Hearing Transcript ("Tr.") p. 10 (testimony of "Philip Morris" ("Morris"), the night manager for

- "ABC"); p. 14 (testimony of "Monk")).
5. On or about December 1, 1992, when preparing the application for an Illinois Business Registration number, taxpayer signed the section of the application that provided, "I accept personal responsibility for the filing of returns and the payment of taxes due." Department Ex. 3, p. 2.
 6. Also on that application, taxpayer identified himself as the only "owner[], general partner[], [or] executive officer" of "ABC". Department Ex. 3, p. 1.
 7. Taxpayer hired his brother-in-law, "Ernie Bilko" ("Ernie"), to manage the day to day operations of the restaurant business. Tr. p. 15 ("Monk"); *see also* Taxpayer Ex. 4 (W-2 Wage and Tax Statements for 1993, identifying "Ernie Bilko" and "Martha Bilko" as employees of "ABC"). "Ernie's" wife "Martha", and his son "Philip" were also employees of "ABC". Taxpayer Ex. 4; Tr. p. 21 ("Monk").
 8. Taxpayer gave "Ernie" a rubber stamp of his, i.e., "Monk", signature to use in the corporation's business. Tr. pp. 15, 18 ("Monk"). "Ernie" used that stamp when signing Illinois tax returns and when preparing checks to pay corporate liabilities, including Illinois tax liabilities. *See* Taxpayer Exs. 3, 8.
 9. Taxpayer regularly went to "ABC's" restaurant to ask "Ernie" about "ABC's" business. Tr. pp. 16-17, 19-20 ("Monk").
 10. "A few times" during those meetings, taxpayer asked "Ernie" to show him "ABC's" corporate books and records, after which "Ernie" would tell him they he didn't know where they were. Tr. p. 17 ("Monk").
 11. Even though taxpayer's signature stamp was used to sign most of the returns filed during the periods at issue, taxpayer personally signed the Illinois sales and use

- tax returns for August and September of 1993, and he also personally signed "ABC" checks drawn to pay Illinois retailers' occupation tax for months during the applicable period, which checks were later dishonored when presented for payment. Taxpayer Ex. 8, pp. 4, 7 (8/93 return and 9/93 return, respectively), 5-6 (check no. 1246, dated 9/20/93), 8 (check no. 1287, dated 10/23/93, and no. 1343, dated 12/20/93); Tr. pp. 28-29, 46-47 ("Monk").
12. Taxpayer's counsel signed taxpayer's name on the Illinois sales and use tax return filed for the month of November 1993. Taxpayer Ex. 8, p. 11; Tr. p. 29 (counsel's comment at hearing). The check drawn to pay the tax shown due on the return for that month was dishonored, also. Taxpayer Ex. 8, p. 12; Department Ex. 1.
 13. In April 1993, two "ABC" checks were written naming "Ernie Bilko" as the payee, each in the amount of \$5,000. Taxpayer Ex. 5, (check no. 1098, written on 4/14/93, and no. 1105, written on 4/28/93). The first check was dishonored on 4/15/93 and on 4/22/93, for insufficient funds. Each check appears to have been written by different persons, and both were endorsed on the back by "Ernie Bilko". *Compare id. with* Taxpayer Ex. 1 ("ABC's" Employer's Quarterly Federal Tax Returns bearing "Ernie Bilko's" signature, as identified by "Monk"); Tr. p. 18 ("Monk").
 14. Another "ABC" check was written in April 1993 naming "Ernie Bilko" as payee, in the amount of \$7,000, which "Ernie" also endorsed. Taxpayer Ex. 5, (check no. 1099, written on 4/15/93). That check appears to have been written by someone other than the persons who wrote the 4/14/93 and 4/28/93 checks to "Ernie". *See id.*

15. On 12/10/93 and on 4/13/94, two more "ABC" checks were endorsed by "Ernie". Taxpayer Ex. 5. The first was written to the order of "CASH", in the amount of \$6,000; the second was written to the order of "Ernie", in the amount of \$3,000. Both checks appear to have been written by "Ernie Bilko". *Compare id. with* Taxpayer Ex. 1.
16. Taxpayer acknowledged that he knew, in July 1994, that "Ernie" had not paid Illinois taxes due from "ABC", and that "Ernie" had also failed to pay other corporate debts. Tr. p. 21 ("Monk").
17. During July 1994, "ABC" received over \$55,000 in gross receipts from selling tangible personal property at retail. Taxpayer Ex. 8, p. 22 ("ABC's" Illinois sales and use tax return for July 1994).
18. None of the \$55,000 "ABC" received during July 1994 was used to pay any of the tax liabilities "ABC" owed to Illinois (*see* Department Exs. 1-2; Taxpayer Ex. 8, p. 22), even though taxpayer had actual personal knowledge that "ABC" had Illinois tax liabilities when "ABC" was earning those July receipts. Tr. p. 21 ("Monk").
19. Taxpayer offered no evidence to show what other assets, that is, assets in addition to the \$55,000 it received during July 1994 (*see* Taxpayer Ex. 8, p. 22), "ABC" had on hand after taxpayer learned of "Ernie's" alleged defalcations.
20. Taxpayer claimed to have lost \$400,000 after "ABC" went out of business. Tr. p. 16 ("Monk"). In July 1994, "ABC's" unpaid ROT liabilities, plus penalties, amounted to approximately \$57,320 (Department Ex. 1, amount of tax and penalties for all periods but for July 1994, which return would be due on August

20, 1994), and its unpaid withholding tax amounted to approximately \$11,000.
Department Ex. 2.

21. Taxpayer offered no evidence that he attempted to use any remaining corporate assets or receipts to pay the tax he knew was due to Illinois after he learned that "Ernie" had failed to pay the tax "ABC" collected from its customers, as well as the taxes withheld from its employees' wages.
22. On 11/11/94, after taxpayer knew that "Ernie" had failed to pay the tax "ABC" collected from its customers, and the taxes withheld from its employees' wages, "Monk" allowed "Ernie" to sign the return "ABC" filed with the Department regarding the gross receipts it realized during the month of July 1994 (Taxpayer Ex. 8, p. 22), and other returns prepared regarding the months of August 1994 through December 1994. Taxpayer Ex. 6; Tr. p. 22 ("Monk", testifying that "Ernie" was "finalizing the company").
23. While the post-July 1994 returns "Ernie" was allowed to sign for "ABC" on 11/11/94 all stated that the "Business [was] foreclosed on 8/1/94 by Bank" (*see* Taxpayer Ex. 6), no documents were offered to corroborate that alleged fact. No evidence was offered to show, e.g., what collateral, including fixtures, receivables, etc., "ABC" or taxpayer may have used to secure any loan that may have been extended to "ABC", or to taxpayer, for "ABC's" business operations.

Conclusions of Law:

When the Department introduced the NOD and NPL into evidence under the certificate of the Director, it presented *prima facie* proof that "Hyeronimous Monk" was personally responsible for the unpaid tax liabilities of "ABC". 35 ILCS 5/904; 35 ILCS

5/1002(d); 35 ILCS 120/13.5 (in effect until 12/31/93); 35 ILCS 735/3-7 (effective 1/1/94);¹ Branson v. Department of Revenue, 168 Ill. 2d 247, 260 (1995) (“by operation of the statute, proof of the correctness of such penalty, including the willfulness element, is established by the Department’s penalty assessment and certified record relating thereto”). The Department’s *prima facie* case is a rebuttable presumption. Branson, 168 Ill. 2d at 262.

After the Department introduces its *prima facie* case, the burden shifts to the taxpayer to establish that one or more of the elements of the penalty are lacking. Branson, 168 Ill.2d at 248. During his opening statement, counsel for taxpayer conceded that taxpayer was an officer for "ABC", but urged that the corporation was run by "Ernie Bilko". Counsel also argued taxpayer cannot be held responsible because "Ernie" deceived taxpayer for 17 months, until July 1994, when taxpayer learned of "Ernie's" non-payment of "ABC's" obligations.

After the Department introduced its *prima facie* case here, taxpayer’s first witness was his nephew, "Philip Bilko". "Philip" is "Ernie Bilko's" son. "Philip" worked for "ABC" from January 1993 through July 1994, as the restaurant’s night manager. Tr. p. 9.² "Ernie Bilko" hired "Philip", and other "ABC" employees. Tr. pp. 9-12. "Philip" knew

¹ While § 13.5 of the Retailers’ Occupation Tax Act (“ROTA”) was repealed with the enactment of the Uniform Penalty and Interest Act (“UPIA”), § 3-9(b) of the UPIA provides that, “[p]enalties shall be imposed at the same rate and in the same manner in effect at the time the tax liability became due.” 35 ILCS 735/3-9(b). Under the ROTA, the rights and liabilities of a corporation, and of the responsible officer(s) of the corporation, accrue at the time the tax becomes due. Sweiss v. Sweet, 269 Ill. App. 3d 1, 6 (1st Dist. 1995). Here, "ABC's" unpaid tax liabilities became due during the period beginning January 1993 through July 1994. Department Ex. 1. Therefore, the provisions of former § 13½ of the ROTA, and of § 3-7 of the UPIA are both applicable to this matter.

² "Philip's" testimony that he was the night manager for the restaurant contradicts "Monk" counsel’s argument that "Ernie Bilko" was the “sole” manager for "ABC". Tr. p. 5.

that taxpayer was the president of "ABC" (Tr. p. 10), and that "Ernie" managed the operations of the restaurant, as well as the employees. Tr. pp. 10-12. He knew that "Ernie" signed "ABC's" checks using taxpayer's rubber signature stamp, and "Ernie" paid the corporation's other liabilities. Tr. p. 11. He testified that "ABC's" sales tax returns were prepared by "Arthur Godfrey", an accountant "Ernie" hired, although he was never present at any meetings where the filing of "ABC's" tax returns were discussed. Tr. pp. 12-13. Finally, he testified that he found out that "ABC" had unpaid liabilities in July 1994, when the restaurant received an eviction notice from the landlord. *Id.*

Taxpayer then testified, and acknowledged that he was the president of "ABC". Tr. p. 14. In response to the question "what were your duties as president?" taxpayer responded:

Really, I wasn't doing nothing because I had a full time job. I was working at "Marv's" Steak House in (city), and I hired "Ernie Bilko" as General Manager and I gave him my stamp, rubber stamp, my signature, and he was doing everything. He was writing, signing the checks.

Tr. p. 15. Taxpayer also testified that he first learned that "Ernie" was not paying Illinois taxes and other corporate obligations in July 1994, when the owner of the restaurant property called him to tell him that he hadn't been paid for two or three months. Tr. pp. 15, 21.

Taxpayer testified that he went to the restaurant at least once every two weeks to ask "Ernie" about "ABC's" business. Tr. pp. 19-20, *see also* pp. 16-17. Taxpayer said that, during those meetings, he always asked "Ernie" whether he was paying "ABC's" taxes. Tr. pp. 19-20. Taxpayer said that "[a] few times" he asked "Ernie" to show him "ABC's" corporate books and records, but that "Ernie" would tell him they he didn't

know where the were. Tr. p. 17. Taxpayer testified that "Ernie" would always tell him, "Don't worry, everything is paid." Tr. p. 20.

Under former section 13½ of the ROTA and current section 3-7 of the UPIA, an officer penalty liability may be imposed upon:

- (1) Any officer or employee of any corporation ... who has the control, supervision or responsibility of filing returns and making payment of ... the tax[es] ... imposed ... **and** who willfully:
- (2) fails to file such return **or**
- (3) [fails] to make such payments to the Department **or**
- (4) ... attempts to in any other manner to evade or defeat the tax

35 **ILCS** 120/13.5; 35 **ILCS** 735/3-7.

Taxpayer contends that while he was an officer of "ABC", he was not a responsible officer of the corporation. *See* Tr. p. 4 (opening statement). I cannot agree. First, taxpayer assumed personal responsibility for filing "ABC's" Illinois tax returns, and paying those taxes, when he signed the applicable section of the application for an Illinois business registration certificate. Department Ex. 3, p. 2. While a responsible officer may delegate the authority to prepare, sign and pay corporate tax returns, sole personal responsibility for seeing that the taxes collected are actually turned over to the state is not, thereby, transferred to the employee to whom authority is delegated. More than one person can be a responsible officer of a corporation. *See* 35 **ILCS** 120/13.5; 35 **ILCS** 735/3-7 (both Acts provide that personal liability may be imposed on "any [responsible] officer or employee ... who willfully fails"). Second, "Monk" hired the person to whom he delegated the authority to sign and pay the corporation's tax returns. Tr. p. 15. While "Ernie" may have had the authority to hire and fire other employees, taxpayer clearly had the authority to hire and fire "Ernie", "ABC's" general manager.

Third, "Monk" actually supervised "Ernie's" activities — although clearly, not very well — by regularly going to the restaurant to meet with "Ernie" and inquire about the operations of the corporation. Tr. pp. 17-20. Finally, "Monk" exercised personal control regarding "ABC's" Illinois tax returns when he signed returns filed during the applicable period, and signed corporate checks drawn to pay the taxes shown due on returns filed regarding the period. Taxpayer Ex. 8. Based on the evidence, I cannot conclude that taxpayer presented evidence that rebutted the Department's presumptively correct determination that "Monk" was an officer of "ABC" who had the control, supervision or responsibility for filing returns and making payment of the taxes imposed on that corporation.

Since "ABC's" withholding and ROT returns were filed, but unpaid, what remains is a determination whether taxpayer either willfully failed to pay the taxes he knew were due, or whether he willfully attempted to evade or defeat the collection of those taxes. As to these elements, taxpayer argued that “there is nothing in the record to indicate ... that Mr. "Monk" knew that Mr. "Bilko" was not mailing the checks to — to whether it be the federal government, state government, or to a creditor. Therefore, he did not know, and he must know to be willful.” Tr. p. 51. Taxpayer went further, and described "Ernie" as a thief who stole from taxpayer, from the business and from other family members. Tr. p. 56.

In Branson, the Illinois Supreme Court addressed and responded to the argument that a responsible officer could not be personally liable for a corporation's taxes where he did not have actual knowledge that taxes were due until the corporation stopped doing business. Branson, 168 Ill. 2d at 266. In that case, the Department, following hearing,

found Carl Branson personally liable for the amount of Carbon, Inc.'s unpaid retailers' occupation taxes for a period from June 1986 through January 1987. Branson, 168 Ill. 2d at 252-53. On administrative review in circuit court, the Department's decision was reversed, because the court found no evidence to establish that Branson willfully failed to pay the taxes due. Branson, 168 Ill. 2d at 253. The Department appealed, following which the appellate court reversed in part and affirmed in part. The appellate court concluded that Branson rebutted the Department's *prima facie* case regarding the period from June through October 1986, before he personally took over the preparation of tax returns. *Id.* The court also concluded, however, that Branson was personally liable for the later periods.

When briefing the specific issue to the supreme court, the Department did not contest the appellate court's conclusion that Branson was not personally responsible for the corporation's unpaid Illinois tax liabilities from June through October 1986. Since the Department did not contest that part of the appellate court's ruling, which the supreme court found "[s]ignificant[]," it did not disturb the appellate court's conclusion on that issue. Branson, 168 Ill. 2d at 267-68. The court, however, continued by noting:

... However, in leaving intact the vacation of the penalty from June 1 through October 31, 1986, we do not intend to imply that a corporate officer who is responsible for filing retailers' occupation tax returns and remitting the collected taxes may avoid personal liability under section 13½ merely by delegating bookkeeping duties to third parties and failing to inspect corporate records or otherwise failing to keep informed of the status of the retailers' occupation tax returns and payments.

We hold that the Department's determination of penalty against plaintiff for the period of November 1, 1986, through January 25, 1987, is not against the manifest weight of the evidence. Although plaintiff claims he did not actually know or become consciously aware of the tax

deficiency until after the business was closed in late January 1987, *lack of willfulness is not proved simply by denying conscious awareness of a tax deficiency that could have been easily investigated by an inspection of corporate records.*

168 Ill. 2d at 267 (emphasis added). While the language in the first paragraph quoted above appears to be judicial dicta (that is, it was not essential to determine the issue the Department waived, *see Cates v. Cates*, 156 Ill. 2d 76, 80 (1993)), the court used that same reasoning as the basis for its holding regarding the period following which Carl Branson had actual knowledge of the corporation's unpaid liabilities. *Branson*, 168 Ill. 2d at 267.

Here, "Monk" testified that he always asked "Ernie" whether he was paying the corporation's taxes. Tr. pp. 19-20. "Ernie", in turn, repeatedly told taxpayer not to worry, that everything was being paid. "Ernie", however, also repeatedly told "Monk" that he didn't know where the corporation's books and records were when "Monk" asked to see them. Answers such as "Ernie's" should foster concern, not alleviate it. "Ernie's" responses should have put "Monk" on notice that the person he delegated to run the corporation's business — using "Monk's" own name — was not a responsible steward for the funds the corporation had collected from its customers, and withheld from its employees.

"Monk", moreover, cannot escape responsibility in this matter merely by pointing the finger at his brother-in-law and crying thief. Contrary to doing "nothing" regarding "ABC's" business (*see* Tr. p. 15), "Monk" personally signed some of the ROT returns "ABC" filed during the applicable period. Taxpayer Ex. 8, pp. 4, 7. He also signed "ABC" checks to pay the tax shown due on those returns. *Id.*, pp. 5, 8. Those checks,

however, were never paid. *Id.* As the person who, in fact, signed his own name asserting that he would assume personal responsibility to see that "ABC's" taxes were paid (Department Ex. 3, p. 2), "Monk" had the duty to see that the corporate checks he personally signed to pay those taxes were honored when presented for payment. Further, "Monk" also allowed his attorney to sign his (i.e., "Monk") name to a return filed during the pertinent period. Taxpayer Ex. 8, p. 11 (return for November 1993). The tax shown as being due, and as having been previously collected from "ABC's" customers, on that return was not paid to the Department, either. *Id.*, p. 12; Department Ex. 1.

Like the court in Branson (*see* 168 Ill. 2d at 267), I conclude that "Monk" has not rebutted the *prima facie* presumption that he acted willfully merely by denying conscious awareness of tax deficiencies that could have easily been investigated by an inspection of "ABC's" records. The corporation's bank statements would have revealed the number of checks that had been dishonored, and an inspection of the corporate checks themselves would have shown that "ABC's" tax liabilities were not being paid.

Even if one believes that "Monk" actually first discovered, in July 1994, that "Ernie" had failed to pay the taxes due on the returns that were filed, there was no evidence offered to show that, thereafter, he attempted to pay any of the amounts due. "Monk" testified that he had an opportunity to talk with "ABC's" accountant in July 1994, who informed him of the different amounts "ABC" owed in taxes and to other creditors. Tr. p. 16, 21. The corporation was still conducting business during July 1994, after "Monk" learned of "Ernie's" alleged defalcations. Taxpayer Ex. 8, p. 22 (return for July 1994). "ABC" earned money from selling food and drink to customers that month, and it continued to collect use tax from the customers it served. *Id.* Whatever "Monk"

decided to do with the cash the corporation had on hand after he learned of "ABC's" tax deficiencies, he used none of it to pay any of the taxes he knew were due.

What "Monk" did instead was to allow "Ernie", the person "Monk" now calls a liar and thief, to sign "ABC's" Illinois sales and use tax return for July 1994, and to file it — unpaid — three months after it was due. "Monk" testified that he lost \$400,000 when the company went out of business. Tr. p. 16. None of that money, however, was used to pay the taxes he knew were due. Department Ex. 1. I conclude that "Monk" failure to pay the taxes he knew were due was willful.

Conclusion:

I recommend that NPL no. 0000 be finalized as issued. I recommend that the tax proposed in NOD no. 0000 for 1993 be assessed and finalized. Interest on both should be assessed pursuant to statute.

Date: 7/27/99

John White
Administrative Law Judge